Earnings Management and Firm Financial Motives
An Empirical Study on Manufacturing Companies in Indonesia

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Abstract

This study aims to determine whether companies with high level of political costs, close to debt covenant violation, issuing equity or bonds, applying a bonus based earnings, achieving and/or exceeding analyst's forecasts, have effect on earnings management. In addition, this study examines whether this relationship are influenced by some company financial conditions, such as the level of profitability, size, leverage, growth, liquidity, and investment. Previous studies generally focus only on one type of motivation to perform earnings management. Therefore, this study enhances the literatures by studying comprehensively various events that may motivate companies to perform earnings management. The results show the level of political costs, bonus based earnings, and benchmarking financial analyst forecasts have significant positive effects on earnings management. Meanwhile, the events of debt covenant violation, issuance of equity or bond have no effect on earnings management. The company financial condition moderated the association between each motive to earnings management, although there is no significant direct impact between financial conditions to earnings management.

Key words: *earnings management, motivation, financial condition*

INTRODUCTION

Earnings information is a component of company's financial statements that aims to assess the performance of management, helps to estimate the use of profit in the long term, as well as assess the risks in investing. Management realized it, so that management tends to do disfunctional behavior by performing earnings management to resolve conflicts that arise between management with stakeholders. Many companies believe that the stock price will increase if the reported net profit increased constantly every year. Therefore, companies management usually choose accounting procedures that produce a certain income to meet the desired targets. The owner also tried to encourage management to maximize their utility in achieving the set targets, with the aim that the entity looks good financially. This practice is known as earnings management.